

# BACHELOR of ECONOMICS



**Thammasat University  
Faculty of Economics  
Bachelor of Economics (International Program)**

## AC201 Fundamental Accounting

Semester 2/2013

### Course Materials

**Topic:**

Chapter 6 Reporting and Interpreting  
Sales Revenue, Receivables, and Cash

**Session:**

Sessions #6

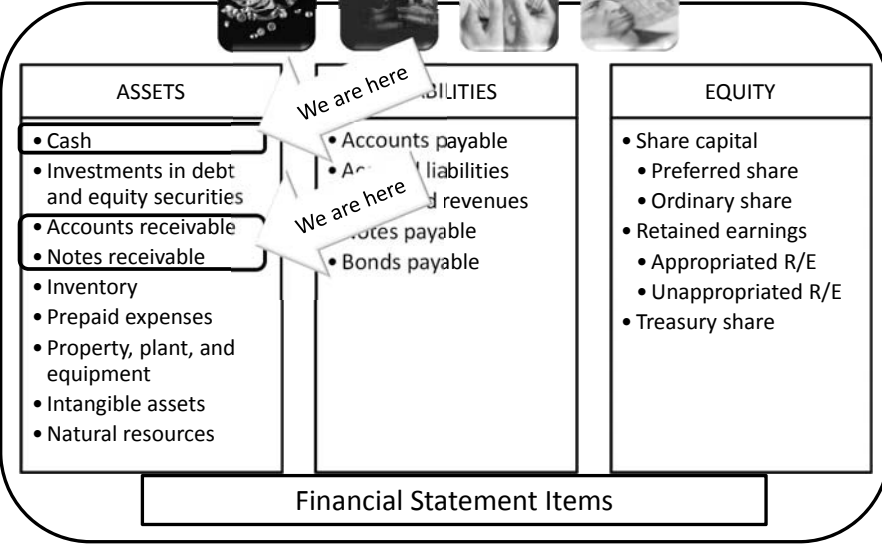
**Instructor:**

Ajarn Santana Singhasaneh



Introduction to Financial Statements

- FINANCIAL STATEMENTS
- ✓ • Statement of Financial Position
  - ✓ • Statement of Comprehensive Income
  - ✓ • Statement of Changes in Equity
  - ✓ • Statement of Cash Flows
- ✓ Accounting Cycle



FINANCIAL STATEMENT ANALYSIS



AC201 Fundamental Accounting



BACHELOR of ECONOMICS

**CHAPTER 6:  
REPORTING AND INTERPRETING  
SALES REVENUE, RECEIVABLES,  
AND CASH**

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## Accounting for Sales Revenue

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## Accounting for Sales Revenue

The revenue principle requires that **revenues** be recorded when **earned**.

1. Goods or services have been delivered.

2. There is persuasive evidence of a customer payment arrangement

3. Price is fixed or determinable.

4. Collection is reasonably assured.

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## Reporting Net Sales

Companies record **credit card discounts, sales discounts, and sales returns and allowances** separately to allow management to monitor these transactions.

Sales revenue
<u>Less:</u> Credit card discounts
Sales discounts
Sales returns and allowances
<hr/>
<b>Net sales</b>

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## I. Credit Card Sales to Consumers

Companies accept credit cards for several reasons:

1. To increase sales.
2. To avoid providing credit directly to customers.
3. To avoid losses due to bad checks.
4. To avoid losses due to fraudulent credit card sales.
5. To receive payment quicker.

When credit card sales are made, the company must pay the credit card company a fee for the service it provides.



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# Recording Credit Card Discounts

On January 2, an adidas factory store’s credit card sales were \$3,000. The credit card company charges a 3% service fee.

GENERAL JOURNAL			
Date	Description	Debit	Credit
Jan. 2	Cash (+A)	2,910	
	Credit Card Discounts (+XR, -R, -SE)	90	
	Sales Revenue (+R, +SE)		3,000
	To record credit card sales and credit card service fee of $\$3,000 \times 3\% = \$90$		

contra-revenue account



# II. Sales Discounts to Businesses

When customers purchase on open account, they may be offered a **sales discount** to encourage early payment.

**2/10, n/30**

Discount Percentage

# of Days in Discount Period

Net (Total sales less returns)

Maximum Days in Credit Period

Read as: **“Two ten, net thirty”**  
The above credit term means the customer can deduct 2% from the invoice price if cash payment is made within 10 days from the date of sales. If cash payment is not made with in 10 day discount period, the full sales price (less any returns) is due within a maximum of 30 days.



## To Take or Not Take the Discount, That is the Question

With discount terms of 2/10, n/30, a customer saves \$2 on a \$100 purchase by paying on the 10<sup>th</sup> day instead of the 30<sup>th</sup> day.

$$\text{Interest Rate for 20 Days} = \frac{\text{Amount Saved}}{\text{Amount Paid}}$$

$$\text{Interest Rate for 20 Days} = \frac{\$2}{\$98} = 2.04\%$$

$$\text{Annual Interest Rate} = \frac{365 \text{ Days}}{20 \text{ Days}} \times 2.04\% = 37.23\%$$



## Recording Sales Discounts

On January 6, adidas sold \$1,000 of merchandise on credit with terms of 2/10, n/30. Prepare the adidas journal entry.

GENERAL JOURNAL			
Date	Description	Debit	Credit
Jan. 6	Accounts Receivable (+A)	1,000	
	Sales Revenue (+R,+SE)		1,000
	To record sales of merchandise on credit		



# Recording Sales Discounts

On January 14, adidas receives the appropriate payment from the customer for the January 6 sale. Prepare the adidas journal entry.

$$\begin{aligned}
 \$1,000 \times 2\% &= \$20 \text{ sales discount} \\
 \$1,000 - \$20 &= \$980 \text{ cash receipt}
 \end{aligned}$$

GENERAL JOURNAL			
Date	Description	Debit	Credit
Jan. 14	Cash (+A)	980	
	Sales Discounts (+XR, -R, -SE)	20	
	Accounts Receivable (-A)		1,000
	To record payment from customer		

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*contra-revenue account* (with arrow pointing to Sales Discounts)



# Recording Sales Discounts

If the customer remits the appropriate amount on January 20 instead of January 14, what entry would adidas make?

Since the customer paid outside of the discount period, a sales discount is not granted.

GENERAL JOURNAL			
Date	Description	Debit	Credit
Jan. 20	Cash (+A)	1,000	
	Accounts Receivable (-A)		1,000
	To record payment from customer		



### III. Sales Returns and Allowances

These situations are recorded in a separate account called **Sales Returns and Allowances**.



**Damaged merchandise.**



**Returned merchandise.**



### Recording Sales Returns and Allowances

On July 8, before paying, a customer returns \$500 of sandals originally purchased on account from adidas.  
Prepare the adidas journal entry.

GENERAL JOURNAL			
Date	Description	Debit	Credit
Jan. 8	Sales Returns and Allowances (+XR, -R, -SE)	500	
	Accounts Receivable (-A)		500
	To record return of merchandise		

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# Reporting Net Sales

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Sales revenue
<u>Less:</u> Credit card discounts
Sales discounts
Sales returns and allowances
<hr/>
<b>Net sales</b>



# Gross Profit Percentage

$$\text{Gross Profit Percentage} = \frac{\text{Gross Profit}}{\text{Net Sales}}$$

In 2009, adidas AG reported gross profit of \$4,712,000 on sales of \$10,381,000.

Gross profit percentage for adidas AG for 2009 is:

$$\frac{\$4,712,000}{\$10,381,000} = 45.4\%$$

COMPARISONS OVER TIME		
adidas		
2007	2008	2009
47.4%	48.7%	45.4%

COMPARISONS WITH COMPETITORS	
Nike	
2009	
46.3%	

Other things equal, higher gross profit results in higher net income.



## Measuring and Reporting Receivables

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## Classifying Receivables

**Accounts receivable**  
are created when companies  
have sales to customers  
on open accounts.

**Notes receivable**  
are written promises  
from another party  
to pay with specified terms.

**Trade receivables**  
are amounts owed to the business  
for credit sales  
of goods or services.

**Nontrade receivables**  
are amounts owed to the business  
for other than business  
transactions.

### Statement of Financial Position Classifications

- **Current (short-term)**
- **Noncurrent (long-term)**

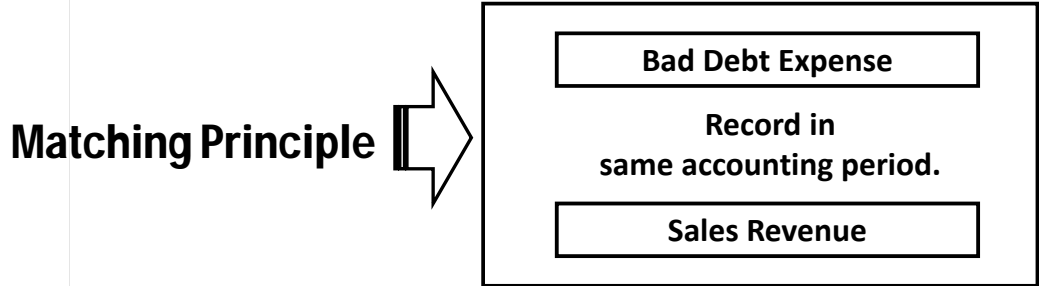
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# Accounting for Bad Debts

**Bad debts** result from credit customers who will not pay the amount they owe, regardless of collection efforts.



Most businesses record an **ESTIMATE** of the **bad debt expense** with an adjusting entry at the end of the accounting period.



# Recording Bad Debt Expense Estimates

adidas estimated bad debt expense for 2009 to be €68,000,000.  
Prepare the adjusting entry.

Bad debt expense (+E, -SE) .....	68	
Allowance for doubtful accounts (+XA, -A) .....		68
<u>Assets</u>	=	<u>Liabilities</u> + <u>Stockholders' Equity</u>
Allowance for doubtful accounts      -68		Bad debt expense (+E)      -68

**Bad Debt Expense**  
is normally classified as a selling expense  
and is closed at year-end.



## Allowance for Doubtful Accounts

Statement of Financial Position Disclosure:

Accounts receivable
<u>Less: Allowance for doubtful accounts</u>
<b>Net realizable value of accounts receivable</b>



Amount the business expects to collect.



## Writing Off Specific Uncollectible Accounts

When it is clear that a **specific** customer's account receivable will be uncollectible, the amount should be removed from the Accounts Receivable account and charged to the Allowance for Doubtful Accounts.

adidas' total write-offs for 2009 were €34,000,000.  
Prepare a summary journal entry for these write-offs.

Allowance for doubtful accounts (-XA, +A) .....	63		
Accounts receivable (-A) .....			63
<b>Assets</b>	<b>=</b>	<b>Liabilities</b>	<b>+ Stockholders' Equity</b>
Allowance for doubtful accounts	+63		
Accounts receivable	-63		